Performance Audit
Revenue Division Document Processing Unit

May 2001

City Auditor's Office

City of Kansas City, Missouri

May 16, 2001

Honorable Mayor and Members of the City Council:

This performance audit of the Revenue Division's Document Processing Unit was initiated by the city auditor pursuant to Article II, Section 13 of the city charter. The performance audit focuses on the timeliness with which the division processes city tax returns and payments.

Posting tax return and payment information to taxpayer accounts takes too long. The majority of tax returns take longer than a month to post, with some returns not posted for over a year. Delays in identifying and notifying taxpayers of tax delinquencies cause penalties and interest to accumulate. Returns for which citizens are owed a refund are processed only after those containing a payment, thus causing the city to hold onto money owed to taxpayers. Only about 60 percent of tax payment checks are deposited promptly. Slow processing also can delay purchasing activity by city departments by delaying contracts with vendors whose tax payments have not yet been recorded.

In addition, the staffing level is not sufficient to prevent a tax-processing backlog during peak seasons. Tax filing deadlines cause almost half of the returns to be received in February, March, and April. Although the staffing level increased during peak periods in 2000, the increase was not enough to prevent a processing backlog. Employee vacancies and high unit turnover resulted in an inexperienced staff, and training and written procedures are inadequate.

The current processing procedures were grafted on to an existing system. The process is cumbersome and inefficient. Errors take a long time to correct. Controls over checks are lax, with orphaned checks not deposited for extended periods, and checks passing through four different stations before they are endorsed.

We make a number of recommendations directed toward reducing the time it takes to post tax return information and deposit checks, including increasing seasonal staffing, outsourcing some processing functions and exploring process alternatives. We also recommend increasing controls over payment checks.

The draft audit report was sent to the director of Finance on March 21, 2001, for review. Management's written response is included as an appendix. We appreciate the courtesy and cooperation extended to us during this project by the staff in the Revenue Division. The audit team for this project was Vivien Zhi, Evalin McClain, and Nancy Hunt.

Mark Funkhouser
City Auditor

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Introduction

Objectives

This audit of the Revenue Division's Document Processing Unit was conducted pursuant to Article II, Section 13 of the Charter of Kansas City, Missouri, which establishes the Office of the City Auditor and outlines the city auditor's primary duties.

A performance audit is an objective, systematic examination of evidence to independently assess the performance of a government organization, program, activity, or function in order to provide information to improve public accountability and facilitate decision-making.[1] This audit was designed to answer the following questions:

- Does the Document Processing Unit process taxpayer documentation and apply payments in a timely and accurate manner?

- Do the Revenue Division's procedures for handling and processing deposits adequately safeguard city assets?

Scope and Methodology

We conducted this audit in accordance with generally accepted government auditing standards, except for completion of an external quality control review of the City Auditor's Office within the last three years.[2] Audit methods included the following:

- Analyzing data from the Automated Revenue System (ARS).

- Reviewing and observing current processing procedures.

- Interviewing city staff, tax administration representatives from other jurisdictions, and payroll company representatives.

- Reviewing literature on tax administration.

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[1] Comptroller General of the United States, *Government Auditing Standards* (Washington, DC: U.S. Government Printing Office, 1994), p. 14.
[2] Our last review was April 1995; a review is scheduled for May 2001.

- Reviewing city documents including management letters, the Code of Ordinances, city regulations, and records relating to personnel, contracts, and tax documentation.

We developed processing times and workload estimates using the receipt dates recorded in ARS. We did additional work to assess reliability of recorded receipt dates after finding instances in which division managers had not verified the dates.

To assess the reliability of the receipt dates recorded in ARS, we compared the date in ARS to the receipt date stamped on the return for approximately 1,000 batches. We reviewed batches that took six or more days to deposit and adjusted receipt dates to match the receipt date stamped on the returns. For returns that were not accompanied by payments, adjusting receipt dates was not feasible.

The longer the length of time between the receipt date and the posting or deposit date, the more frequent the variation in receipt dates. However, because the groupings used for analyzing the data are broader as the time to process or deposit lengthens, our estimated posting and deposit times are not materially affected. In addition, most returns are received within a period consistent with their filing deadlines. We believe that the adjusted data is reasonably reliable for the purposes for which we used it.

No information was omitted from this report because it was deemed privileged or confidential.

Background

Legislative Authority

The city's authority to impose and collect taxes is found in Article I of the city charter. Article IV of the charter assigns responsibility for the administrative oversight of taxes to the Finance Department, with the Revenue Division responsible for collecting fees related to certain licenses, permits, and taxes.

Taxes Collected by Revenue Division

The Revenue Division directly collects wage earner, profits, utility, convention and tourism, and occupational license taxes.

Wage earner tax. All Kansas City residents and non-residents working within the city are liable for a one-percent earnings tax. Employers maintaining an office or transacting any business within Kansas City are required to withhold earnings tax. Nonresident employers may establish voluntary withholding accounts. Individuals whose taxes are fully withheld by their employers are not required to file a return. Employers remit withholding payments 4 to 48 times per year, file a return quarterly, submit W-2 information for each employee, and complete a final return annually. Wage earner tax returns and payments are required annually from those individuals whose taxes are not fully withheld by their employer.

Profits tax. The city levies a tax on business net profits of resident entities as well as nonresident entities doing business in the city. All businesses are required to file regardless of taxable income. Profits returns and payments are required annually.

Utility tax. The city imposes license and franchise fees on companies that sell electricity, natural gas, steam and chilled water for heating and cooling, telephone service, and cable television. The quarterly license fees are based on gross receipts.

Convention and tourism tax. The city levies hotel and restaurant taxes based on sleeping room charges (excluding sales tax) paid by transient guests of hotels, motels, and tourist courts, and gross receipts derived from restaurant retail food sales. Hotels and restaurants remit convention and tourism taxes 1 to 48 times a year, on the same schedule as the state sales tax.

Occupational license tax. Chapter 40 of the Code of Ordinances identifies the businesses that must be licensed. The base on which the tax is calculated and the rates applied vary by business type. Returns are filed annually.

Tax Collection Revenues

In fiscal year 2000, the Revenue Division collected over $256 million in tax revenues, or about 55 percent of the city's total tax revenues. Between fiscal years 1996 and 2000, the Revenue Division's tax collections increased about 12 percent. The relative proportion of revenues produced by each tax type remained stable, with wage earner and profits taxes representing approximately 57 percent. (See Exhibit 1.)

Exhibit 1. Tax Revenues Collected by Revenue Division, FY 1996-2000 (In Thousands)

Tax Type	1996	1997	1998	1999	2000
Wage Earner & Profits	$127,184	$134,873	$139,253	$145,694	$146,958
Utility	65,283	68,909	66,576	69,688	68,371
Convention & Tourism	21,457	20,901	22,564	22,970	24,393
Occupational License	14,450	15,447	12,117	14,219	16,490
Total	$228,374	$240,130	$240,510	$252,571	$256,212

Sources: CAFR 2000 and Revenue Division records.

Number of Tax Accounts

The number of tax accounts administered by the Revenue Division increased by 43 percent between fiscal years 1996 and 2000. More than 50,000 tax accounts were added during the five-year period. (See Exhibit 2.)

Exhibit 2. Number of Revenue Division Tax Accounts, FY 1996-2000

Tax Type	1996	1997	1998	1999	2000
Wage Earner & Profits	99,152	107,836	106,255	120,645	139,533
Utility	18	20	28	35	45
Convention & Tourism	1,057	1,083	1,067	1,127	1,237
Occupational License	16,267	15,525	23,173	23,355	26,009
Total	116,494	124,464	130,523	145,162	166,824

Source: Revenue Division records.

Authorized Positions and Staffing Expenditures

Authorized staffing levels declined 15 percent between fiscal years 1996 and 2000. The division eliminated 11 positions in fiscal year 1998 due to the consolidation of managerial level positions and the anticipated use of new technologies. Personal services expenditures declined by 7 percent between fiscal year 1996 and 2000. (See Exhibit 3.)

Exhibit 3. Personal Services Expenditures and FTE, FY 1996-2000

Fiscal Year	Personal Svcs. Exp.	FTE
1996	$2,277,502	80
1997	2,261,039	82
1998	2,092,399	68
1999	2,130,499	69
2000	2,123,509	68
Change from 1996-2000	-7%	-15%

Sources: Adopted Budgets, 1998-2002, and AFN.

Document Processing Unit

The Document Processing Unit is one of four units within the Revenue Division. The unit is under the supervision of a document processing

manager. The front-end processing supervisor oversees seven full-time employees who receive and process payments and returns. A data entry/quality control supervisor oversees six full-time employees who verify and correct scanned information, and manually enter non-scannable information and payment applications. Temporary and contract employees and an information processing vendor also assist in entering tax information into the city's tax system. (See Appendix A for an organizational chart of the division.)

ARS and Imaging System

The city installed the Automated Revenue System (ARS), an integrated tax administration system, in August 1992. It includes six subsystems: taxpayer identification, returns processing, taxpayer accounting, case management, correspondence architecture, and revenue accounting. ARS is a major component of the Kansas City Financial Management System (KCFMS). ARS is based on Andersen Consulting's TAS (Tax Administration System) software.[3]

Revenue Division staff enter information into ARS by two methods: scanning and manual entry. Tax and payment information for most wage earner, profits, withholding, convention and tourism, and occupational tax accounts is obtained through scanning the return, check, and supporting documentation. The imaging system was brought on-line in May 1998. Returns are scanned and released to the image server. Scanned return information is verified in the imaging system before it is uploaded into ARS.

Staff manually process irregular, high dollar, and time sensitive returns. In calendar year 2000, only about 14 percent of items posted were processed manually. Utility payments, which are typically large dollar payments, are a processing priority in order to speed up the bank deposit. Bill payment applications, which represent a majority of the manual processing activity in 2000, are a priority in order to decrease the possibility of issuing erroneous bill notices. Extension requests, cigarette taxes, wire transfer, and collection agency information are also manually entered.

See Appendix B for a chart of the document processing unit's workflow.

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[3] Proquire, formerly a part of Andersen Consulting, supports the ARS software. Proquire has informally advised the city that in five years, it will no longer support the software.

Findings and Recommendations

Summary

The Revenue Division's Document Processing Unit takes too long to post tax return and payment information to taxpayer accounts. The majority of tax returns take longer than a month to post, with some returns not posted for over a year. Delays in identifying and notifying taxpayers of tax delinquencies cause penalties and interest to accumulate; returns for which citizens are owed a refund are processed only after those containing a payment; and taxpayers may be asked to provide copies of previously submitted returns or canceled checks when information is not available on the system. Slow processing also can delay purchases by city departments.

The Document Processing Unit's staffing level is not sufficient to prevent a tax-processing backlog during peak seasons. Tax filing deadlines cause almost half of the returns to be received in February, March, and April. Although the staffing level increased during peak periods in 2000, the increase was not enough to prevent a processing backlog. Employee vacancies and high unit turnover resulted in an inexperienced staff, and training and written procedures are inadequate. Management should increase the variable staffing level to more closely match the flow of returns and payments. In addition, outsourcing withholding payment processing would reduce the need for additional staff. Improved training and updated written procedures could also help improve overall tax processing speed.

The current processing procedures were intended to streamline tax processing and enforcement. However, the scanning technology, which was grafted on to the previous process, has not produced anticipated efficiencies. Posting is slow and errors take a long time to correct. Performance measures should be developed to increase management's knowledge about unit activities and provide information to help in future decision making and planning. Management should identify opportunities to improve current processes, as well as explore paperless processing alternatives.

Finally, control weaknesses over checks could contribute to the risk of loss or theft of city funds. Orphaned checks can sit for extended periods and are neither endorsed nor deposited until the appropriate individual account has been identified. A clearing account should be set up and

used for orphaned checks and all checks should be restrictively endorsed on receipt.

Processing Delays Affect Taxpayer Perceptions and Other City Processes

Processing tax documentation and payments takes too long. The majority of tax returns take longer than a month to post, with some returns not posted for more than a year. Slow posting of tax information negatively impacts taxpayer perceptions, particularly when penalties and interest accumulate or when refunds are delayed. Slow processing also delays the deposit of tax payments and the issuance of tax clearance letters.

Posting Is Slow

Posting return information to taxpayers' accounts is slow. It can take more than a year to post some tax information to ARS. In 2000, less than half the returns were posted within 30 days after they were received, while 7 percent of the returns took six or more months to post. (See Exhibit 4.)

Exhibit 4. Cumulative and Median Days to Post Returns (By Quarter)

Days to Post	1st Qtr.	2nd Qtr.	3rd Qtr.	4th Qtr.	Total Year
Within 5 Days	10%	5%	9%	15%	9%
Within 10 Days	33%	9%	16%	23%	20%
Within 20 Days	47%	14%	28%	44%	32%
Within 30 Days	53%	26%	53%	68%	46%
Within 40 Days	58%	32%	67%	81%	55%
Within 60 Days	68%	43%	79%	92%	66%
Within 90 Days	80%	61%	90%	98%	79%
Within 180 Days	91%	87%	99%	100%	93%
Median Days[4]	25 days	68 days	28 days	21 days	35 days
No. of Returns	81,341	87,488	46,371	44,241	259,441

Source: Adjusted ARS Data.

Second quarter returns take longer to post. The Revenue Division posted returns received in the second quarter of 2000 more slowly than returns received during the other three quarters. The median days to post a return received in the second quarter was 68. The median days to post a return received during the rest of the year was under 30. The slower posting in the second quarter is related to the higher, concentrated

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[4] The median is the middle number or value in an ordered set of given numbers. The median days to post represents the midpoint in the range of days to post values, with 50 percent of the returns posting in fewer days and 50 percent of the returns posting in more days.

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volume of returns received in April and a backlog of unposted first quarter returns.

Slow Processing Impacts Taxpayer Perceptions

Taxpayers' perceptions of customer service can be impacted negatively by slow processing. Tax payments are an obligation. Taxpayers expect accurate information and timely processing of their tax payments and returns. When slow processing causes penalties and interest to accumulate, refunds to be delayed, and documents to be resubmitted, taxpayer perceptions regarding service will suffer.

Slow processing increases the penalties and interest owed by taxpayers. Taxpayers identified through Revenue Division enforcement actions as owing additional taxes are liable for the tax, penalty, and interest accruing from the time the original tax was due. Delays in identifying and notifying delinquent taxpayers result in additional penalties and interest. Taxpayers who may have been unaware that they owed taxes, who made calculation errors, or whose taxes were improperly withheld may not realize that additional taxes are due until an enforcement action is initiated. Taxpayers have complained to city officials that they would have paid their tax liability sooner had they been notified sooner.

The length of time to post a return is one of several factors that influence when an enforcement action is initiated. Other factors include the staffing levels in the Revenue Division's enforcement unit and the availability of matching information from the Internal Revenue Service.

Processing priorities slow the refund process. Returns that include payments are processed first. Although the division has an objective of processing refunds within 10 weeks of receipt, refund processing is not the highest priority. Other taxing jurisdictions pay interest on refunds that are not processed within a specified time frame. Kansas City, however, does not pay interest on refund money owed to taxpayers.

Some jurisdictions use incremental processing procedures to post payment information prior to posting and verifying the entire return. Kansas City's Revenue Division, however, uses batching and scanning returns as a cash deposit control. The division ties the posting and depositing of tax payments to the processing of the associated return. Returns are scanned in batches, and deposits are expected to match the dollars included in the batch. As a result, payments and returns with payments are processed before returns for which a citizen is owed a refund.

Slow processing burdens taxpayers and increases division workload.
Posting delays result in incomplete or inaccurate taxpayer information.
Taxpayers who report they filed their taxes and paid the related tax
liability but whose information is not reflected in ARS are requested to
resubmit copies of documentation. Duplicate submissions add to the
processing workload. Any related enforcement case is placed on hold
pending the posting of additional information.

Slow Posting Affects Other City Processes

Slow processing delays deposit of checks received. Although the
division makes depositing larger checks a processing priority, deposit
delays limit the city's access to collected revenues. Slow posting can
also delay the issuance of tax clearance letters provided to vendors,
which in turn slows the city's purchasing process.

Next-day deposit requirements are not met. About 60 percent of
checks received are deposited on or before the next business day. (See
Exhibit 5.) Section 2-200 of the Code of Ordinances requires that
monies be paid into the city treasury on the next business day following
the day of collection for deposit in a banking institution. The Revenue
Division's daily procedures also require that all money be deposited the
next day, except for checks that are received without sufficient
documentation to apply to specific accounts.

Exhibit 5. Days to Deposit 2000 (By Quarter)

Days To Deposit	1st Qtr.	2nd Qtr.	3rd Qtr.	4th Qtr.	Total Year
0 Day	2%	3%	1%	5%	3%
1 Day	60%	45%	61%	80%	59%
2 Days	23%	14%	21%	6%	16%
3 Days	3%	9%	6%	1%	5%
4 Days	6%	5%	4%	3%	5%
5 Days	3%	4%	3%	2%	3%
6-10 Days	2%	20%	2%	1%	8%
11-15 Days	1%	0%	1%	1%	1%
16 Days or More	1%	0%	1%	1%	1%

Source: Adjusted ARS data.

The time between when a taxpayer makes a payment and when the city
deposits the check should be minimized. Checks should be deposited as
soon as possible in order to maximize available funds, increase interest
earnings, decrease the likelihood of a payment becoming a bad check,
and meet taxpayer's expectations that checks will be processed promptly.

Larger checks are a processing priority. The Revenue Division's first priority is to deposit receipts. Staff reports that they attempt to identify and expedite processing and depositing of larger checks. The staff also tries to give priority to processing returns that typically generate larger individual check payments.

In 2000, the deposit pattern of checks processed by the Document Processing Unit reflected the unit's emphasis on depositing larger checks. About 3 percent of checks were deposited on the date received. These checks represented approximately 18 percent of check dollars processed. About 91 percent of the checks were deposited within 5 days of receipt, reflecting 96 percent of total check dollars. The total number of check transactions and the average check size generally declined as the number of days to deposit increased. (See Exhibit 6.)

Exhibit 6. Days to Deposit and Transaction Volume

Days to Deposit	Percent of Checks Deposited	Percent of Amount Deposited	Deposit Amount	Average Check Amount
0 Day	3%	18%	$ 43,850,544	$ 8,866
1 Day	59%	57%	139,412,719	1,228
2 Days	16%	12%	29,082,715	923
3 Days	5%	3%	8,076,866	828
4 Days	5%	3%	7,715,798	872
5 Days	3%	2%	4,925,379	802
6-10 Days	8%	3%	8,292,471	532
11-15 Days	1%	0%	742,706	507
16 Days or More	1%	0%	814,368	679

Source: Adjusted ARS Data.

Slow posting can cause city purchasing delays. The city's current purchasing system requires vendors to supply departments making purchases a tax clearance letter that certifies that the vendor is current with city tax obligations. Slow posting of information to the ARS system can delay the issuance of clearance letters.

The Revenue Division prepares tax clearance letters. Letters are provided to vendors based on a review of tax records. When the records reviewed do not show a payment or a filing, the division may request that the vendor supply copies of supporting documentation. Vendors who have usually complied with the city's tax requirements are informally provided a three-month window to compensate for posting delays. Vendors who have not historically complied with their tax obligations must supply copies of documentation prior to the issuance of the clearance letter if the current records show missing filings or postings.

Slow posting can delay the purchasing process and result in inconsistent treatment of vendors.

According to managers in some city departments, the city's tax clearance process is holding the city's purchasing and contracting processes hostage. Slow posting places a burden on vendors and departments making purchases. The difficulties with the tax clearance process, however, extend beyond the issues of slow posting. A Kansas City Government Optimization (KC-GO) committee has examined the tax clearance process and recommended revisions to the process.

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Mismatched Staffing and Workload Cause Backlogs

Tax filing deadlines cause seasonal fluctuations in workload that contribute to slow posting. Although 45 percent of returns are received during February, March, and April, staffing levels do not increase to adequately match workload volume. Vacancies and high turnover during 2000 resulted in an inexperienced work force, which also contributed to posting delays. Finally, limited training and outdated written procedures worsen the problem.

Workload Is Seasonal

About 45 percent of returns are received during February, March, and April due to the April 15 filing deadline for wage earner and most profit returns and the February 28 deadline for occupational license. Withholding returns, which represent 48 percent of all returns processed, are spread out over the year but peak quarterly. Convention and tourism returns also peak quarterly. KC payments are evenly distributed throughout the year.[5] (See Exhibit 7.)

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[5] KC payments include bill payments as a result of enforcement activities and payment applications.

Exhibit 7. Returns Received by Month, Calendar Year 2000

Month	Occupation License	Wage Earner	Profits	Withholding	C&T	KC Payments	Other[6]	Total	Number of Returns
Jan	14%	1%	2%	8%	6%	9%	9%	7%	17,690
Feb	**36%**	10%	5%	**13%**	**11%**	10%	12%	**13%**	34,972
Mar	**28%**	15%	15%	6%	9%	10%	13%	**11%**	28,679
Apr	7%	**67%**	**49%**	7%	5%	9%	6%	**21%**	54,287
May	4%	2%	3%	**12%**	**12%**	8%	5%	8%	21,505
Jun	2%	1%	3%	5%	7%	8%	5%	5%	11,696
Jul	2%	1%	3%	8%	6%	7%	5%	5%	14,097
Aug	2%	1%	4%	**11%**	**10%**	8%	5%	8%	19,665
Sep	2%	1%	5%	6%	8%	7%	3%	5%	12,609
Oct	2%	1%	7%	7%	7%	8%	5%	6%	15,233
Nov	1%	0%	1%	**12%**	**10%**	9%	12%	7%	19,093
Dec	1%	0%	1%	5%	9%	8%	19%	4%	9,915
Returns	25,047	39,014	29,999	124,754	11,865	28,047	715	100%	259,441

Source: Adjusted ARS Data.

Concentrated receipt of returns slows processing. The concentration of returns in a relatively short period of time produces a backlog of work that requires months to process. Returns filed for occupational license, wage earner, and profits taxes are processed more slowly than returns for taxes that do not have a single peak period. The median days between receipt and posting is substantially longer for return types with a peak period than for returns that are received throughout the year. (See Exhibit 8.)

Exhibit 8. Median Days to Post by Return Type

Major Return Type	Median Days to Post	Number of Returns
Occupational License	67	25,047
Wage Earner	69	39,014
Profits	77	29,999
Convention and Tourism	34	11,865
Withholding	29	124,754
All Return Types	35	259,441

Source: Adjusted ARS Data.

Peak periods slow deposits. The concentration of returns received in April contributes to the slow posting of second quarter receipts. During 2000, about 20 percent of returns with checks were received in April. Only about a fourth of individual April payment checks were deposited by the next business day and approximately a third of the payment checks were held at least six days before deposit. Concentrated receipt of checks results in processing and deposit delays. (See Exhibit 9.)

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[6] "Other" includes utility and cigarette taxes.

Exhibit 9. Days to Deposit, April 2000

Days To Deposit	Percent	Cumulative Percent
0 Day	3%	3%
1 Day	21%	24%
2 Days	18%	41%
3 Days	12%	53%
4 Days	7%	61%
5 Days	6%	67%
6-10 Days	32%	99%
11-15 Days	0%	100%
16 Days or More	0%	100%

Source: Adjusted ARS Data.

Staffing Does Not Match Workload

In 2000, staffing levels did not match the processing workload. Based on the number of regular unit employees at the end of each month and converting temporary, and contract staffing resources to full-time equivalents (FTEs), the Document Processing Unit's average monthly staffing level was 18 FTEs in 2000.[7] Staffing peaked in April at 21.5 FTEs and was lowest during August and September with about 15 FTEs.

Staffing increases during peak periods but not enough. The peak April staffing level reflected an increase of 3.5 FTEs, or only 19 percent more than the yearly average. The number of returns received in April, however, was 196 percent higher than the average number of returns received during the other months. The number of returns received per FTE reflects the imbalance between workload and staffing. This imbalance resulted in slow posting times for returns typically received during peak periods. (See Exhibit 10.)

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[7] The Document Processing Unit employee full-time equivalent positions were based on month-end employment and were not adjusted for leave, vacation, and overtime. We did not include hours contributed by city employees from other units. Conversion for temporary and contract staffing as full-time equivalent positions is based on a 40 hour work week.

Exhibit 10. Number of Returns Per FTE by Month

Returns Per FTE
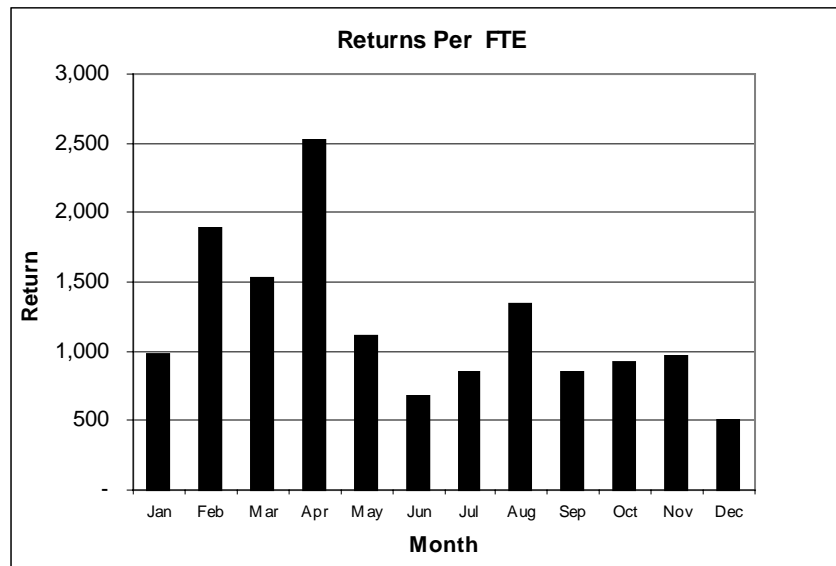
Sources: Adjusted ARS Data and Staffing Data.

High Employee Turnover Further Impacts Backlog

The Document Processing Unit's voluntary employee turnover rate was 41 percent in calendar year 2000, substantially higher than the city's overall rate of 13 percent. In calendar year 2000, six employees resigned.

The Document Processing Unit was never fully staffed in 2000. Although 13 hourly positions were authorized, one to four of these positions were vacant each month. The front-end section is now fully staffed with seven employees. Five of these employees, however, were hired during 2000. In the data entry section, one of the six positions is vacant, and two of the remaining six hourly employees have been with the city for less than a year.

Lack of formal training impacts productivity. The high turnover rate resulted in a high number of new employees in need of training. Most of the training offered to new employees is on-the-job training, which may not be adequate. Systematic training regarding the ARS and imaging system is not provided. The lack of formal training limits employees' knowledge and understanding about the functions they are expected to perform.

Policies and procedures are outdated. Most available documentation for the Document Processing Unit was written in 1995 and 1996 before the scanning system was brought on-line. Some of the current documentation consists of hand-written notes. Updated written

procedures are needed to provide a source of information that could be referred to when questions arise and provide a basis for training.

Complete written instructions on work procedures would provide a valuable reference for employees. Without proper training and a complete set of written instructions, employees may not be fully informed about their responsibilities or the procedures they are required to follow. The director of Finance should take steps to ensure that a more systematic program of employee training is developed and division policies and procedures are updated.

Outsourcing and Increasing Variable Staffing Could Improve Processing Speed

Two changes in the way the Revenue Division handles tax receipts have the potential to improve processing speed. Outsourcing withholding payment voucher processing through the use of electronic funds transfer and a lock box could reduce the amount of paper processing required in the Document Processing Unit and could cut one day from the current deposit schedule. An increased level of variable staffing could be used during the first half of the year to increase the speed of return processing.

Use of electronic funds transfer could ease the workload. In order to reduce the volume of mail and paper processed, and to increase deposit speed, the division should explore two bank-based processing alternatives: electronic funds transfer and traditional lock box processing.

Employers' withholding payment vouchers account for approximately 28 percent of the returns processed in 2000. The monthly withholding payment vouchers are very simple documents that are typically mailed with a withholding payment. The only information included on the voucher is the account identification, period, and payment amount. Although the Document Processing Unit easily scans these documents, an outside bank could process them.

Payroll companies submit the majority of withholding activity processed by the city. Representatives of three payroll companies with whom we spoke reported that although they did not typically provide monthly and annual reconciliations electronically, they did submit monthly withholding payments and filings electronically to the IRS and to some state and local jurisdictions.

The payroll company representatives disagreed on whether program development and testing of electronic filings and payments would be

difficult to establish. One payroll representative stated that electronic transfers via ACH (Automated Clearing House) would not be used for withholding processing unless the firm was mandated to do so. This reluctance to electronically transfer payments and data may be a reflection of complex programming expenses or may be a reluctance to lose the float on payment monies being held by the payroll company.

Lock box processing could be used for withholding payments.
Traditional lock box processing is an alternative for organizations that process their own payroll but do not have experience using electronic transfers of data and payments. The city could contract with a bank to process payments and convert paper return information into a prescribed electronic format. Although Revenue Division personnel indicated that their experience with lock box processing has been unsuccessful in the past, establishing specific performance standards in the contract and monitoring the information received closely could help to ensure performance quality.

Outsourcing withholding payment voucher processing should free staff to process more complex transactions. In addition, the electronic transfer of payments and information or a traditional bank lock box should increase the speed with which funds are deposited into a city interest-bearing account. The director of Finance should take the steps necessary to outsource the processing of withholding payment vouchers.

Increased variable staffing is needed to match workload.
Management should more closely match staff to workload needs by substantially increasing seasonal staffing. In order to handle workload during periods of peak activity, the Document Processing Unit hires temporary employees and contractors, and requires mandatory overtime. In April 2000, seven temporary employees were hired to process mail. In addition, city employees from outside of the Document Processing Unit also assisted during peak periods. The additional staffing, however, did not match the workload.

Based on the fiscal year 2000 workload, we estimate that the Document Processing Unit would need 20 FTEs or 7 employees in addition to its authorized positions in order to match staffing to workload for January, February, March, and May, and 40 FTEs or 27 additional employees in order to meet the workload in April. (See Exhibit 11.) Our analysis assumed that withholding payments processing would be outsourced, as we recommended. The estimate for January includes time to train and familiarize temporary employees with the job responsibilities and procedures they are to perform, while April staffing levels assume that an additional shift would be added to the unit's work schedule. Based on

current processes, adding the recommended staff would reduce median posting time to 23 days, with 90 percent of returns posted within 62 days of receipt. The director of Finance should increase the variable staffing levels to more closely match the workload in the Document Processing Unit.

Exhibit 11. Number of Returns Per FTE After Recommendation
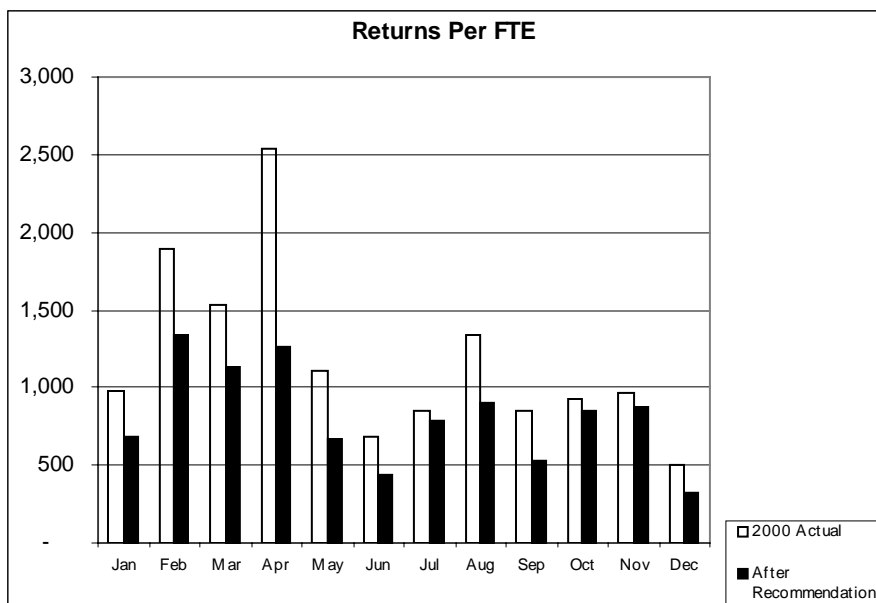
Sources: Adjusted ARS Data and Staffing Data.

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Front-End Process Is Cumbersome

The Revenue Division's imaging system was intended to minimize the need to key data manually while improving data accuracy, providing better service, improving overall efficiency, and enhancing enforcement and audit functions. Two tax years after the scanning process was grafted on to the previous manual processing system, however, return processing is still slow and the anticipated efficiencies have not been realized. Scanning, verifying, and correcting scanned returns take more time than originally anticipated.

Revenue Division staff told us that they believe scanned documentation saves time by enabling customer service and enforcement employees to retrieve and view copies of taxpayer documents electronically. Taxpayer and processing mistakes, however, slow posting. Because errors take a long time to correct, information in the ARS system is not current for all accounts.

Current City Scanning Technology Is Limited

The most efficient use of scanning equipment is when a taxpayer submits a return on an original city form. City-supplied forms contain preprinted codes and carefully aligned boxes to improve the accuracy with which the scanning equipment can read and record taxpayer-supplied information. When information is word-based rather than number-based, is not submitted on an original city return, or requires a large number of supporting attachments, scanning as a method of entering specific items of information becomes less advantageous.

Scanning requires document preparation and verification.
Documents must be prepared for processing before the scanner can be used to capture data or images. All documents are batched by return type, return year, and date received. In some instances, additional preparation is necessary to ensure that the system is able to recognize the return type. W-2s, which are typically printed on thin paper, must be taped to a sturdier 8 ½ x 11 paper before scanning. Before items are uploaded into ARS, each return is reviewed and verified by employees. Key pieces of return information obtained through the scanning process are highlighted for verification, as are inaccurate calculations.

ARS Information Is Compromised Until Error Files Are Corrected

Taxpayers make mistakes when preparing returns and employees make processing mistakes. The ARS processing system has controls in place to reject or suspend information that does not match or meet certain system criteria. Until errors are corrected, however, the information on ARS is incomplete and inaccurate.

Batch errors reject before posting to ARS. On average, about 47 percent of the items that were scanned, verified, and ready to be posted to ARS were put into an error file based on a review of 23 days of the suspended counts from the scan error file report and the scanned file records read reports. Batch processing provides controls over the information that is entered into ARS. When established controls or checks and balances of the system are not met, the entire batch is rejected. Controls include matching the dollar total of the batch, valid characters, and valid period dates. Returns rejected at the batch level are placed in an error file.

Items that cannot be applied to taxpayer accounts are suspended.
When items meet the batch level controls, they are uploaded into ARS.
However, when an item cannot be applied to an individual account
within ARS, the item is suspended. We reviewed 22 business days of the
suspense reports and the posted transactions reports. On average, 22
percent of the individual items that uploaded to ARS were suspended.
Of the items that uploaded or suspended during the days examined, about
17 percent were suspended because of account errors, such as incorrect
taxpayer information, dates, and periods, and about 3 percent were
suspended because of untimely or missing postings.

Mistakes take a long time to correct. Considerable time is expended to
identify and correct rejected and suspended items. It is sometimes
necessary to research records or investigate accounts. Although
corrections may be made to a single return, in other instances rebatching,
rescanning, and accounting adjustments are necessary.

Error file corrections can take more than a year to correct. The error
file is a raw data file that only the data entry section supervisor and the
document processing manager can access and correct. On October 13,
2000, 4,824 items were in the error file; by January 12, 2001, the number
of items on the error file had dropped to 1,633. Until a batch error is
corrected, all items within the batch remain unposted, and return or
payment information is not available for customer service or
enforcement's use. Some of the items contained in the October 2000
error file were scanned as early as April 8, 1999, more than 18 months
previously.

Number of suspended items remains high. The November 11, 2000,
suspended transaction summary included 7,781 items in the suspense
file. Over 40 percent of the suspense items in the file had been
suspended for more than 36 days. As of January 2, 2001, there were
5,486 items in the suspense file.

Opportunities to Improve Processes Should Be Explored

The processing system and procedures used in the Document Processing
Unit have not eliminated the backlog of unposted information. Scanning
technology that was grafted onto a pre-existing tax information system
has yet to produce anticipated efficiencies. Performance measures that
could be used to evaluate processing performance have not been
established.

The current process should be evaluated. The current scanning
system was grafted onto a pre-existing tax information system. The

integration of ARS and scanning technology has resulted in a complex and cumbersome process. Processing improvements, which were originally anticipated to be achieved through the use of scanning, have not been realized. The current process needs to be evaluated based on the initial two years of process experience, performance information, and available improvements in systems and technologies. The director of Finance should review the current paper processing and scanning processes to identify procedural and process changes or alternatives that would improve processing activities.

Performance measures should track posting and correction times.
The Revenue Division does not track the time to post return information to a taxpayer's account and the time to correct suspended items. Although the Document Processing Unit receives several daily reports, most of these are production reports. Clearly stated and consistently monitored performance measures would provide management with better information about staff and process performance that could be used to help in decision-making. Progress as measured by these performance measures should be reported, and used to determine whether procedures are effective or need to be improved. The director of Finance should establish performance measures for document processing.

Staff should continue to explore paperless processing alternatives.
Electronic transfer of data can reduce processing costs, errors, and delays associated with paper-based information processing. The technology and processes used in tax administration vary widely. Programs vary in scope and complexity. Taxpayers vary in their readiness to accept and utilize new technologies. There is no single best solution for taxing agencies. Taxing agencies are, however, taking steps to decrease paper-based processing.

The IRS and state of Missouri are currently expanding various electronic filing initiatives. The IRS has developed a number of paperless filing alternatives both internally and in conjunction with commercial software developers. The federal government has also joined forces with some states to allow taxpayers to file joint federal and state returns electronically. Other states have developed their own electronic filing systems.

The Revenue Division budget for fiscal year 2002 includes funding to introduce and test a form of Internet e-filing. The division has also investigated other electronic filing, payment, and information related initiatives. Over the long run, technological innovations are critical to improving the timely processing of returns. Because of the large dollar volume, the involvement of a large number of individuals and entities,

and the need to obtain accurate information from filers, the director of Finance should continue to explore and promote electronic processing alternatives.

Revenue should post ACH transactions electronically. Some employers transmit withholding payments and information electronically via ACH. Until recently, the division had requested that the city's bank fax the information submitted in support of electronic payments. Although the city now retrieves the information electronically, Revenue continues to manually post some of these transactions. In order to gain the full advantages of electronic data transmissions, payment information should be posted electronically whenever possible. The director of Finance should direct that staff work with employers and Information Technology to identify format adjustments that need to be made in order to permit the electronic application of ACH payments to taxpayers' accounts.

Controls Over Assets Could Be Strengthened

Control weaknesses contribute to the risk of loss or theft of city funds. The Revenue Division does not deposit orphaned checks – negotiable checks received without documentation – until the account to which the payment is to be applied is identified. Checks pass through four different processing stations before they are endorsed. Unendorsed and undeposited checks are susceptible to loss and misappropriation.

Orphaned Checks Should Be Deposited Into a Clearing Account

The Revenue Division does not deposit checks that are received without accompanying documentation until employees investigate and identify the account to which the payment should be posted. On October 13, 2000, the Revenue Division held unposted and unendorsed orphaned checks totaling $8,866. The largest check was for more than $6,800 and had been received more than two weeks before.

The Government Finance Officers Association suggests establishing a clearing account to handle checks lacking the information necessary to apply the funds to an appropriate account. Problem checks should be deposited in a bank if they appear to be negotiable, with the money allocated internally to the clearing account pending final disposition. The money can be allocated to the proper fund and account once it is identified. The director of Finance should establish a clearing account to handle checks that lack the information necessary to apply the funds to an appropriate account.

Checks Should Be Endorsed on Receipt

The division does not restrictively endorse checks when received. Checks move through four processing stations before a restrictive endorsement is applied. The division routinely holds unendorsed checks overnight and may not endorse orphaned checks for weeks. Checks that are not endorsed on receipt contribute to a weak control environment.

Promptly endorsing checks provides a basic control over city receipts. KPMG's 2000 Management Letter recommends that the first employee to handle a check apply the restrictive endorsement. The city's current cash handling instruction and management authorities[8] recommend the immediate restrictive endorsement of checks. Although access to the document processing area is restricted and sorting, batching, scanning, and microfilming take place in open areas, unendorsed checks are susceptible to loss and misappropriation. The director of Finance should ensure that checks are restrictively endorsed on receipt.

Recommendations

1. The director of Finance should develop a systematic training program and update document processing policies and procedures.

2. The director of Finance should outsource withholding payment voucher processing.

3. The director of Finance should increase the variable staffing levels to more closely match the workload in the Document Processing Unit.

4. The director of Finance should review the current paper processing and scanning processes to identify technological improvement or process alternatives.

5. The director of Finance should establish performance measures for the Document Processing Unit.

6. The director of Finance should continue to explore and promote electronic processing alternatives.

7. The director of Finance should direct staff to take the steps necessary to permit the electronic application of ACH payments.

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[8] Wanda A. Wallace, *Handbook of Internal Accounting Controls*, (Englewood Cliffs, NJ: Prentice-Hall, Inc., 1991), p. 184, and Municipal Treasurers' Association of the United States and Canada, *Internal Controls Checklist*, (Washington, DC, 1994), p. 42.

8. The director of Finance should establish a clearing account to handle orphaned checks.

9. The director of Finance should ensure that checks are restrictively endorsed on receipt.

Appendix A

Revenue Division Organizational Chart

FINANCE DEPARTMENT
Revenue Division

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                              ┌─────────────────────┐
                              │  Manager of Revenues │
                              └─────────────────────┘
                    ┌──────────────────────────┐
                    │ Analysis / Administration │
                    │        Analyst III        │
                    └──────────────────────────┘
                         │ Analyst II
                         │ Analyst I
                         │ Admin Asst I
                           Secretary
```

Document Processing Analyst III	Enforcement / Audit Analyst III	Bus License / Taxpayer Assistance Analyst III

Front End Processing Customer Serv Spvr	Quality Control / Data Entry Customer Service Spvr	Audit Analyst II	Enforcement	Business License Admin/Asst II	Taxpayer Assistance Customer Serv Spvr

Front End Processing — Customer Serv Spvr
- Secretary
- Secretary
- Secretary
- Secretary
- Secretary
- Secretary
- Secretary

Quality Control / Data Entry — Customer Service Spvr
- Secretary
- Secretary
- Secretary
- Secretary
- Secretary
- Secretary

Audit — Analyst II
- Municipal Rev Agent II
- Municipal Rev Agent II
- Municipal Rev Agent II
- Municipal Rev Agent II
- Municipal Rev Agent II
- Municipal Rev Agent II

Enforcement

Section I Customer Service Spvr	Section II Customer Service Spvr	Section III Customer Service Spvr	Post Legal / Bankruptcy Admin Asst III
Customer Service Rep	Customer Service Rep	Customer Service Rep	Municipal Rev Agent II
Customer Service Rep	Customer Service Rep	Customer Service Rep	Admin Asst II
Customer Service Rep	Customer Service Rep	Customer Service Rep	Information Processor
Customer Service Rep	Customer Service Rep	Customer Service Rep	
Customer Service Rep	Customer Service Rep	Customer Service Rep	
	Customer Service Rep	Customer Service Rep	

Business License — Admin/Asst II
- Customer Service Rep
- Customer Service Rep
- Customer Service Rep
- Customer Service Rep
- Customer Service Rep
- Customer Service Rep
- Customer Service Rep

Taxpayer Assistance — Customer Serv Spvr
- Customer Service Rep
- Customer Service Rep
- Customer Service Rep
- Customer Service Rep
- Customer Service Rep

Source: Revenue Division, 5/01.

Appendix B

Document Processing Work Flow

Revenue Division Document Processing Work Flow

Start

Mail opened and sorted

Scannable returns and payments

Non-scannable returns

Checks received without returns, or checks received with more than one type of return or tax year, and bill payments

Scannable returns and payments are sorted by return type. Return and check are clipped together. If the amount indicated on the return and check differ, the check amount is written on the return. Returns without payments are stamped "no payments".

Non-scannable returns and payments are sorted by return type. Return and check are clipped together. If the amount indicated on the return and check differ, the check amount is written on the return. Returns without payments are stamped "no payments".

Returns and payments are sorted into batch by type of return and year and by stock and preprinted returns (up to 30 items per batch).

Returns and payments are sorted into batch by type of return and year up to 30 items per batch).

Front-end processing runs tapes of dollars on checks and returns on each batch and fills out the batch header card.

Front-end processing runs tapes of dollars on checks and returns on each batch and fills out the batch header card.

Returns and payments are scanned by batch.

Does the number of returns in each batch match the number shown on the scanner?

Rescan

No

Yes

Scanner assigns batch ID and prints ID on the back of each return and check.

Scanned return information is queued for manager review.

Front-end staff researches item and applies payments.

A notice prints out after each payment application.

Batch IDs are manually assigned and stamped on the front of checks and returns/payment application notices.

Returns and checks are separated. Each has a tape of dollar totals to go with it.

The checks and batch cards are endorsed and microfilmed by endorser.

A file folder is made for each batch.

File folders of the returns to be manually entered are taken to the Data Entry section.

File folders for scanned returns are stored in the vault. Batch information is recorded in a log book.

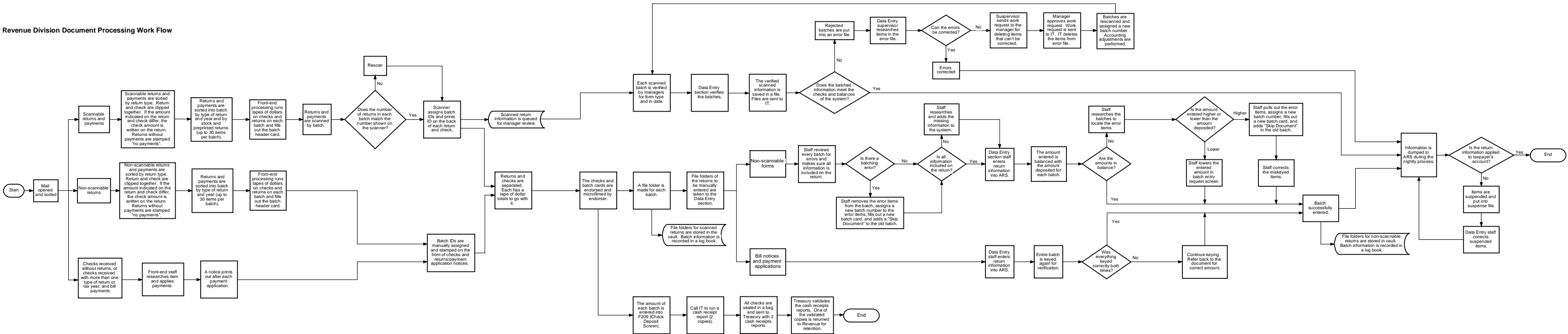Each scanned batch is verified by managers for form type and in date.

Data Entry section verifies the batches.

The verified scanned information is saved in a file. Files are sent to IT.

Does the batched information meet the checks and balances of the system?

No

Yes

Rejected batches are put into an error file.

Data Entry supervisor researches items in the error file.

Can the errors be corrected?

Yes

No

Errors corrected

Supervisor sends work request to the manager for deleting items that can't be corrected.

Manager approves work request. Work request is sent to IT. IT deletes the items from error file.

Batches are rescanned and assigned a new batch number. Accounting adjustments are performed.

Non-scannable forms

Bill notices and payment applications

Staff reviews every batch for errors and makes sure all information is included on the return.

Is there a batching error?

No

Yes

Staff removes the error items from the batch, assigns a new batch number to the error items, fills out a new batch card, and adds a "Skip Document" to the old batch.

Is all information included on the return?

No

Yes

Staff researches and adds the missing information to the system.

Data Entry section staff enters return information into ARS.

The amount entered is balanced with the amount deposited for each batch.

Are the amounts in balance?

Yes

No

Staff researches the batches to locate the error items.

Is the amount entered higher or lower than the amount deposited?

Higher

Lower

Staff lowers the entered amount in batch entry request screen.

Staff corrects the miskeyed items.

Staff pulls out the error items, assigns a new batch number, fills out a new batch card, and adds "Skip Document" in the old batch.

Batch successfully entered.

Information is dumped to ARS during the nightly process.

Is the return information applied to taxpayer's account?

Yes

No

End

Items are suspended and put into suspense file.

File folders for non-scannable returns are stored in vault. Batch information is recorded in a log book.

Data Entry staff corrects suspended items.

Data Entry staff enters return information into ARS.

Entire batch is keyed again for verification.

Was everything keyed correctly both times?

Yes

No

Continue keying. Refer back to the document for correct amount.

The amount of each batch is entered into the F209 (Check Deposit Screen).

Call IT to run a cash receipt report (2 copies).

All checks are sealed in a bag and sent to Treasury with 2 cash receipts reports.

Treasury validates the cash receipts reports. One of the validated copies is returned to Revenue for retention.

End

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Appendix C

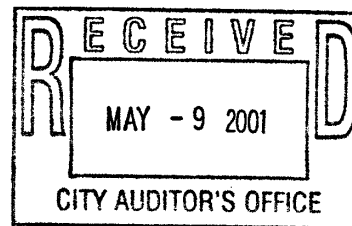
Director of Finance's Response

Interdepartmental Communication

DATE: May 9, 2001

TO: Mark Funkhouser, City Auditor

FROM: Kevin Riper, Director of Finance

SUBJECT: Performance Audit on the Revenue Division Document Processing Unit

I appreciate the opportunity to review and respond to the draft of the Performance Audit on the Revenue Division Document Processing Unit prepared by the City Auditor's Office. The report contains nine recommendations directed to the Finance Department. The Finance Department's response to those recommendations is set forth below.

Recommendation Number 1 – The director of Finance should develop a systematic training program and update document processing policies and procedures.

Agree

The Finance Department agrees with the City Auditor's conclusion that the training program for the Document Processing section of the Revenue Division should be strengthened and that its procedures should be updated.

Currently the division utilizes a great deal of on-the-job training to train both new employees and temporary staff. Given the resources available, on-the-job training is the most efficient and productive method to train staff. Although there is significant turnover in the area, the section has only thirteen line staff positions, and therefore rarely hires more than one individual at any given time. As such, it is not feasible, nor does the division have the available resources to conduct a formalized training "class" for each new employee. Temporary staff as well as employees borrowed from other areas, are generally trained to complete only a limited number of the tasks performed by full time Document Processing section employees. Depending on the number of individuals being trained, the division utilizes either short classes or on-the-job training for the particular task(s) they will be completing.

The City Auditor points out that many of our current procedures were written in 1994 and 1995. These procedures were written subsequent to the installation of the Automated Revenue System (ARS) still being used in the Revenue Division. Although the division subsequently implemented its document management (imaging) system, the imaging system feeds into ARS. Therefore, the ARS procedures are still valid. The division has

made progress in preparing documentation related to those procedures specific to the imaging system. The division will continue to move toward insuring that all of the relevant imaging procedures are fully documented, and that all of its document processing procedures are incorporated into a single procedures manual that will be utilized as part of its training processes.

The division will also move toward utilizing technology to make training materials more accessible by placing them on-line. As recognized by the Audit Report, the turnover in the Document Processing section is significant. This turnover results in a loss of institutional knowledge. By providing more accessible resource and training materials, the Revenue Division hopes to counter some of the negative effects of turnover in the Document Processing section.

Recommendation Number 2 – The director of Finance should outsource withholding payment voucher processing.

Agree

The Finance Department agrees that outsourcing withholding payment vouchers would reduce the current workload of the document processing staff and allow them to concentrate on some of the more complex tax returns received and ultimately improve overall processing speed. The department will study available outsourcing options for processing withholding payment vouchers, including a bank lockbox operation as well as electronic payment options.

Currently the Revenue Division is accepting withholding payments via the Automated Clearing House (ACH) system. In calendar year 2000, the division collected approximately $22 million dollars or about 8.5% of the revenue collected by the Revenue Division via ACH. Currently, the items received via ACH must still be manually posted to taxpayers' accounts. The division is working to improve this process to incorporate an Electronic Data Interchange (EDI) component so that payments are received with the appropriate addenda records that can be uploaded electronically into ARS. This will eliminate both the need to manually post items received via ACH and the need for taxpayers to submit paper returns.

Recommendation number 3 – The director of Finance should increase the variable staffing levels to more closely match the workload in the Document Processing Unit.

Agree

The Audit Report estimates that between 7 and 27 additional FTE are necessary during the period from January to April to meet the workload during that timeframe. In a section consisting of 13 front line FTE, adding 7 to 27 additional FTE during peak processing

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periods will be a significant management challenge. Currently the Revenue Division does attempt to meet seasonal staffing needs through several mechanisms. As indicated in the Audit Report, the division utilizes both temporary and contractual employees during its peak season. In addition, employees within other sections of the Revenue Division also spend a considerable amount of time during the division's peak season assisting the Document Processing section and overtime is regularly offered. The Revenue Division also typically schedules six mandatory Saturdays during the months of March, April and May. On each of these mandatory Saturdays, approximately one-half of the division's permanent employees work an eight hour shift processing tax returns. Temporary staff and contractual employees also work these Saturdays as do employees from other divisions within the Finance Department.

Even so, the Finance Department agrees that current staffing levels are not adequate, especially during peak processing times. The Director of Finance will explore opportunities for additional staffing through the further redeployment of existing permanent positions, the use of contractual and temporary staffing, and, perhaps eventually, additional permanent positions. A large increase in seasonal staffing will also increase the Revenue Division's requirements for office space, equipment, and supervisory personnel. The Audit Report assumes that an additional shift, would be added in the Document Processing section in order to accommodate the increased staffing. While this would limit some of these additional requirements, a shift differential for those employees working a "non-standard" shift may be needed to attract and retain employees. Requiring current employees to work a "non-standard" shift may prove to be a de-motivating factor and could further increase turnover in the section.

Recommendation number 4 – The director of Finance should review the current paper processing and scanning processes to identify technological improvement or process alternatives.

Agree

This recommendation underscores the Finance Department's original vision when it proposed implementing the imaging system that it currently uses. The Revenue Division's imaging system was intended to serve as an intermediate step as it moved toward electronic as opposed to manual processes. Although the imaging technology implemented in 1998 did not produce all the efficiencies anticipated, using this technology is more efficient than manually processing all tax returns.

As recognized by the Audit Report the number of returns and amount of revenue processed by the division has increased significantly during the past 5 years. In order to keep pace with these increases, improved technology is critical. Some of the technologies the Finance Department is exploring for tax processing include e-filing and 2D bar coding. Both technologies are compatible with the Revenue Division's current infrastructure, and are currently being used by other tax administration agencies. For

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example, the Missouri Department of Revenue, which is currently using 2D bar coding, is very pleased with this rather inexpensive technology and is actively working with tax software providers to increase its use.

Recommendation number 5 – The director of Finance should establish performance measures for the Document Processing Unit.

Agree

Performance measures are an indispensable tool in monitoring and evaluating workload, throughput, speed, accuracy and customer understanding. As part of the Revenue Division's commitment to performance measurement, divisional managers attended a conference in November 2000 specifically devoted to performance measurement in tax and revenue administration. Currently the Revenue Division is in the process of developing performance measurements and reports to systematically track a number of the items addressed in the Audit Report, including the length of time it takes to deposit funds received and the length of time it takes to post tax returns to taxpayer accounts. The division currently tracks outstanding suspended items and is working to refine the report to track the age as well as the number of such items.

The division is also reviewing document processing standards from other tax administration agencies, including the State of Missouri, and will incorporate those standards as benchmarks in developing its performance measurements. While the Finance Department recognizes that it takes a significant period of time to develop good measures of organization performance,[1] the Director of Finance is committed to measuring and improving performance in the Document Processing section.

Recommendation number 6 – The director of Finance should continue to explore and promote electronic processing alternatives.

Agree

The Finance Department believes that electronic processing of tax returns is one of the most viable mechanisms to substantially reduce the amount of time needed to process tax returns, and that one of the top priorities of the City-wide e-commerce initiative should be e-filing of tax returns. There are numerous options available today for electronic tax filing, and the Revenue Division has begun to study these options. The document management system currently used by the division has a component that could be added to the existing system, allowing for internet based e-filing of returns. As noted in the response to recommendation number two, the Revenue Division currently receives about 8.5% of its payments via the ACH system. The division is not only pursuing improving

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[1] Studies from the United States General Accounting Office indicate it takes five to ten years for an organization to acquire an acceptable level of competence in measuring organization performance.

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its use of this system to include an EDI component, but is also interested in expanding its use of the ACH system. While not all of the taxpayers the Revenue Division deals with are interested in electronic filing options, and as recognized by the Audit Report it may be necessary to mandate some changes, electronic processing is critical to reducing processing cost, errors and delays. The Director of Finance will continue to investigate electronic alternatives for tax administration and will seek the necessary resources to develop and support such initiatives.

Recommendation Number 7 – The director of Finance should direct staff to take the steps necessary to permit the electronic application of ACH payments.

Agree

The Finance Department agrees that the electronic application of payments received via ACH is a critical next step in its efforts to move toward electronic as opposed to manual processes. As noted in the response to recommendations number two and six, the Revenue Division currently receives about 8.5% of its payments via the ACH System, and is working with the Information Technology Department to improve the process to incorporate an Electronic Data Interchange (EDI) component. This will eliminate the need to manually post these items, allowing a reallocation of resources to other tasks.

Recommendation Number 8 – The director of Finance should establish a clearing account to handle orphaned checks.

Agree

The Finance Department recognizes that it is preferable to process all funds upon receipt, even in those cases when further research is needed to properly post the monies to the correct taxpayer account. The Revenue Division will work with the Accounts Division of the Finance Department and the Information and Technology Department to establish a clearing account and appropriate procedures so that orphaned checks can be deposited upon receipt.

Recommendation Number 9 – The director of Finance should ensure that checks are restrictively endorsed on receipt.

Agree in part

The Finance Department agrees that immediate restrictive endorsement is preferable to delayed endorsement, and, after implementing the other recommendations in this audit, will explore ways to change or, conceivably, eventually replace the Revenue Division's current accounting and document processing systems to accommodate immediate

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restrictive endorsement of checks. Unfortunately, moving to immediate restrictive endorsement at this time without changing the current accounting and document processing systems would further delay the deposit of funds and the posting of returns, thus reducing tax liability accuracy – all negative impacts whose costs are significantly greater than the benefit of immediate restrictive endorsement.

Under the division's current accounting and document processing systems, the reason the checks are not endorsed immediately upon receipt is that to do so would require physically separating the checks from the accompanying tax returns, breaking the critical link between the tax returns and the accompanying check. It would be extremely inefficient to physically remove the checks, restrictively endorse them and reattach them to the respective returns so that they can be batched and imaged together.

Batching like returns together is necessary to meet the requirements of the division's accounting system. The Revenue Division processes funds for several different revenue sources. Batch processing of returns/checks is necessary to insure that funds received are posted to the correct revenue source in an efficient and effective manner. If the checks were separated from the returns prior to batching, the Revenue Division would lose many of the checks and balances now utilized when making the daily deposit and make it nearly impossible to post revenue to the correct source and to locate errors that occur. Therefore it is critical that the returns and checks remain together until they are imaged in the division's document management system.

In addition, separating the checks from the returns prior to scanning them through the document imaging system would prevent the return and check from being imaged simultaneously. This would preclude the unique identifying number from being printed on the checks and the returns and would eliminate the link within the Revenue Division's archived records between a particular return and the check that was received with it. This link within the archived records is used for research purposes and to detect errors that have occurred. Eliminating the link created by the imaging system would make it impossible to research particular payment and posting errors after the fact.

The Auditor's recommendation that checks be immediately endorsed upon receipt serves to underscore the soundness of the Auditor's recommendation for electronic filing alternatives to eliminate as much of the burdensome processing of physical returns and checks as possible.

cc: Wanda Gunter, Deputy Director of Finance
       Tracy Smedley, Commissioner of Revenue
       Eric Davison, Manager of Document Processing

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